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Financial Markets

Irving Trust

Irving Trust Company
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New York, NY 10015

Economic Research &
Planning Division

Friday
(Noon)

Oct. 17, 1980

Most market rates were unchanged to modestly higher, on balance, during the holiday-shortened week, as some reversals of earlier rate reductions set in late in the week. Substantial differences of opinion continued to exist among market participants with respect to the likely near-term movement of interest rates, adding to the generally nervous character of the markets.

Rates in the Treasury sector fell slightly Wednesday afternoon, primarily reflecting the surprise of some participants at the Federal Reserve's move that day to purchase Treasury bills for its own account. Unfortunately, an outright System purchase should not have come as a surprise (it was anticipated in this letter two weeks ago), as it was required primarily to counter the seasonal reserve-draining impact of increases in currency in circulation that occur about this time of year. The purchase could have been done a week earlier without complicating open market operations; but by Wednesday, there was little choice. With a large volume of RPs having been arranged during the statement week ended Wednesday, and with a modest reserve-adding week about to commence on Thursday, the Fed faced the prospect of arranging a huge amount of RPs in coming weeks if it did not supply reserves via an outright purchase. The Fed took the reasonable course. Even so, the size of the transaction was apparently considerably less than called for by the seasonal need, and thus the Fed--as demonstrated by Thursday's four-day RPs--is not yet out of the RP business. Whatever the Fed's motives for this approach, the market can look forward to additional outright purchases sometime in the next couple of weeks. Once again, however, the operation will be of a technical nature and will not necessarily indicate a change in the Fed's policy stance.

Our view is that the current target for net borrowed reserves is about $1.2 billion--a level consistent with funds trading at about 12 1/2% or a little higher. Even if the money stock should register substantial declines in the next few weeks, it would be hard to get the funds rate much under 12%. That emphasizes a problem highlighted in last week's letter: Treasury bill rates currently are well below financing rates, reflecting the expectation of at least some market participants that the funds rate will decline--fast! However, this expectation is likely to be frustrated, and thus the bill sector seems especially vulnerable to a continuation of the interest rate backups, which set in late this week. Other market instruments, carrying substantially higher rates than bills of comparable maturity, are not so exposed.

The FOMC meets on Tuesday, October 21. Since M-1B is just under the top of its target range, while no very palpable signs of a business slowdown have yet appeared, the prospect is that the committee will vote to leave monetary policy substantially unchanged. We continue to expect rate declines by year-end, however.

William C. Melton

Note: The full text of this letter is available to Telerate subscribers on pages 7250-51 on the Monday morning following the Friday date of the letter.

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Market Yields

	10/17/80	Week Ago	Year Ago
Prime Lending Rate at Irving Trust Company	(Noon)		
Short-term loans to substantial depositors with highest credit rating	13.50%	13.50%	14.50%
Effective since	10/1/80		
Discount Rate at Federal Reserve Bank	11.00	11.00	12.00
Federal Funds	12.63	12.88	13.75
Repurchase Agreements	12.30	12.25	12.25
U.S. Treasury Issues			
Bills			
3 months	11.55	11.55	12.75
6 months	12.13	11.88	13.25
1 year	12.10	11.95	12.60
Coupons			
2 years	11.86	11.60	12.10
4 years	11.69	11.55	11.15
7 years	11.55	11.47	10.70
10 years	11.57	11.40	10.60
Long Bond	11.38	11.20	10.00
Negotiable Certificates of Deposit-Secondary Market			
1 month	12.60	12.40	13.75
3 months	12.70	12.50	14.15
6 months	12.70	12.50	14.50
1 year	12.70	12.50	13.75
Banker's Acceptances			
1 month	12.60	12.50	13.75
3 months	12.40	12.50	14.50
6 months	12.00	12.55	14.80
Eurodollar Deposits			
1 month	13.13	12.88	14.00
2 months	13.31	12.88	14.63
3 months	13.38	12.94	14.88
Commercial Paper - Prime Names			
Directly placed by:			
Finance Companies			
1 week	8.00	12.00	12.00
1 month	12.25	12.00	13.25
3 months	11.50	11.25	12.75
Bank Holding Companies			
1 month	12.25	12.50	13.13
Dealer Placed:			
3 months	11.90	12.25	13.38
New AA Corporate Utility Bond	13.50	13.25	11.25
Tax Exempt			
6 month Project Notes	5.25	5.20	5.90
1 year AAA Bond	5.90	6.00	NA
5 year AAA Bond	6.20	6.30	NA
20 year AAA Bond	8.15	8.20	6.95

This information represents prevailing market yields.
It should not be construed as an offering.
All yields are on the offered side of the market.

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